

# ICPS newsletter

## JPMorgan: Ukraine's investment attractiveness is underestimated

*During their business trip across Ukraine, a group of foreign investors, together with experts of the world-famous investment company JPMorgan, met with economists from ICPS in order to exchange opinions on the current economic situation in Ukraine. In particular, the experts were interested in the growth forecasts for the Ukrainian economy for the next few years, the main factors in this growth, the prospects for improvement of the investment climate, and the effects of the political situation on the country's economy*

During the meeting, the ICPS economists presented their perspective on Ukraine's economic development during 2003–2005, which, in their opinion, would be characterised by the following features:

- with no significant reforms being carried out, Ukraine's GDP growth will settle at 3.5–4.5% per year;
- in anticipation of the forthcoming presidential elections, investment growth will fall off, while the galvanisation following the elections will be augmented by the effects of enterprise privatisations during 2003–2004 and the lifting of restrictions on land sales starting in 2005;
- the upswing in domestic demand growth will remain, with the personal income tax reforms expected in 2004 contributing to this trend;
- owing to a conducive foreign economic situation and expanded distribution markets for Ukrainian products, Ukrainian exports will increase, although the breakdown will be dominated by goods with low levels of processing and by raw materials;
- imports will outperform exports, spurred by improved household consumption;
- the deflation reported in the YE'02 results is not likely to prove the rule in upcoming years, which will be characterised by price rises following higher salaries and softer monetary and fiscal policy prior to the presidential elections.

The foreign investors also sought to find out what ICPS economists considered to be the drivers of and risks to further economic development in Ukraine. The following is a

summary of important questions and answers during the meeting:

**JPM:** This year, the government's forecast for GDP growth is 7%, so what has prompted the pessimism in the ICPS forecasts?

**ICPS:** The government assumptions are based on the 7% growth observed in January. We believe that this figure reflected seasonal fluctuations and do not anticipate that such a buoyant dynamic will persist. Above all, we expect no perceptible progress with economic reforms, and we also take account of the impact upon the economy of the upcoming presidential elections, as a factor which will willy-nilly involve big business.

**JPM:** What do you think the pre-election risks, if any, imply? Why are fewer foreign direct investments forecasted prior to the elections, when Ukraine's prospects worldwide are looking up?

**ICPS:** The risk is that the outcome of the struggle for power between different political and economic cliques will be property re-distribution. Furthermore, foreign investors rarely venture to Ukraine without having established strong ties with domestic business; therefore, the risk of domestic businesses losing their influence may affect their overseas partners, as well.

**JPM:** As for the volumes of foreign direct investments, do you have knowledge as to what amounts of incoming money are re-invested into already created foreign-capital enterprises, what belongs to new companies coming to Ukraine, and what sectors of the economy will the bulk of this money be invested in?

**ICPS:** The bulk of foreign investments is channelled into the food industry and retail trade. Unfortunately, more detailed

### Announcement

During 11–13 June 2003, Kharkiv will host the Ukraine National Conference on Local Economic Development with sponsorship from the USAID. The primary goal of the conference is to promote discussion of major factors affecting regional and local economic development in Ukraine. The conference aims to foster cooperation among all government levels, business oriented NGOs and the business community to achieve the common goal of business development and improved local and regional economies.

Conference themes:

- implementing regulatory reform in the spheres of regional and local economic development to enhance business formation and growth;
- creating a favorable investment environment at regional and local levels and improving business access to short and long-term credit;
- using strategic planning for regional and local development; examples, best practices and results;
- institutionalizing economic development practices: establishing local economic development offices (EDOs), NGOs, and regional agencies and associations; experience exchange, best practices, successful examples.

Through workshops and roundtable discussions participants will create a short list of high priority actions needed to support rapid sustainable local economic development throughout Ukraine. This list will be offered for adoption at the final plenary session of the conference and included in the conference proceedings.

Conference participants will be National and Local government representatives, business community representatives, leaders of Ukrainian NGOs working on regional and local economic development issues, and representatives of international organizations and diplomatic missions.

Applications for participation in the conference are accepted till 14 March 2003. If you are interested in more information about the conference, please contact the Academy for Educational Development by email: [lead@aed.kiev.ua](mailto:lead@aed.kiev.ua) or fax: 380-44/230-2672.

information about incoming investments is unavailable. Judging from the investment sources, we can also assume that the majority of incoming money is actually Ukrainian money, repatriated to the country of origin via offshore zones.

**JPM:** What is your opinion on the recent statement regarding the creation of an economic union between Belarus, Kazakhstan, Russia, and Ukraine?

**ICPS:** The creation of such a union envisages the promulgation of a common foreign economic policy—which, first of all, contradicts Ukraine's focus on European integration; and secondly, we consider this move to be premature, especially due to the lack of corresponding institutions that would support the activities of this economic union. If so, the union would be threatened by the lack of coordination at a political level or the domination of one country over others. We believe that existing agreements on free trade should suffice.

**JPM:** Central European countries are gradually integrating into the EU, with the first-wave and second-wave countries of EU

enlargement almost having been determined. Do you see Ukraine in the third wave of EU enlargement?

**ICPS:** Certainly this is a possibility in the next 10–15 years; however, our forecasts do not span such a long term. Despite the President of Ukraine having declared the necessity of undertaking gradual measures to create real prerequisites for EU accession by Ukraine in 2011, there are great risks that this program will not be accomplished, in particular, due to the necessity of profound changes in the ideology of the country's economic policy—and those are the most difficult changes of all.

When commenting on their overall impressions regarding Ukraine, Michael Marrese, Department Manager for Economic Research and Public Strategy in the CEE, JPMorgan, said:

– Most importantly, we discern a tremendous potential here. At this time, it has been roughly estimated that the legal economy accounts for only half of the real production, while the government has finally

acknowledged the need to expand the tax base in order to curtail the volume of the shadow economy. However hopeless it might seem at first sight, we can cite many encouraging examples of combating shadow economy: over the past five–six years, Bulgaria and Turkey have achieved exceptional progress. Russia is another example: four years ago, it would never have crossed anybody's mind that Gazprom or leading oil companies would be paying such large volumes of taxes. We perceive the same potential in Ukraine. If we look upon Ukraine as investors, we will see that it has minor external debts and relatively high returns, while in Central Europe investment opportunities are shrinking, because EU candidate countries have already brought in European legislative norms, which do not encourage the business environment. For this reason, I would say that you underestimate your country's investment potential. ■

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## Project launched to analyse the effectiveness of NGO management

***Each year, the performance of NGO management plays an increasingly important role in the stability of organisations and their further development. However, information about the activities of such bodies and their system of functioning is scanty. The clarification of governing bodies' role in maintaining the stability of non-profit organisations, along with a scrutiny of their work systems, is the topic of research carried out by BoardSource (USA), jointly with the GURT Resource Centre and the International Centre for Policy Studies***

The research is conducted under the framework of the Program for Facilitating the Management of Non-Profit

### ***What is an effective management body?***

*Effective management bodies run their organisations based on transparent decision making, during which the managers of non-profit organisations undertake to efficiently allocate and utilise resources, and exercise their authority based on common values and principles. The key advantages bestowed by effective management on their organisations are the following:*

- *stability;*
- *reasoned decision making;*
- *identification of goals and visions;*
- *effective organisational planning;*
- *efficient resource management;*
- *boosting the organisation's standing in the public eye;*
- *improvement of programs and services.*

Organisations of Ukraine, carried out by BoardSource—one of the leading global resource centres for training materials and information about NPO management. The project's goal is to facilitate the management of non-profit organisations in Ukraine by equipping management bodies, executive directors, employees, and other stakeholders with the necessary knowledge and instruments for establishing more transparent and stable organisations.

The unified methodology, applied in all Central and Eastern European countries, envisages a sociological survey by post among third-sector representatives across all the regions of Ukraine concerning management principles and execution in their organisations, based on the results of which a policy report will be drawn up. The focus of the research will be on the role and activity of the highest-rank managerial bodies of the organisations—the official bodies having legitimate authority and

responsible for decision making with regard to the most essential aspects of the organisations' activity. In particular, such bodies include supervisory boards, boards of directors, general assemblies, conferences, etc.

In the next several weeks, non-profit organisations of Ukraine will receive questionnaires regarding the activity of their organisations' management teams. We would be grateful if they would return the questionnaires with their answers as soon as possible. All the information volunteered therein is confidential and will only be used for generalising the research results. Organisations involved in the research will receive the policy report with aggregate research results, to be published in summer 2003. The report will also contain information about the role and duties of management bodies of Ukrainian non-profit organisations, which may facilitate the development of new programs and projects. All organisations that participate in the research will also receive a new publication focusing on management issues that is being compiled for publication by BoardSource and the GURT Resource Centre.

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